

United States. Thus, if this section applies with respect to a partnership for a taxable year solely because the tax matters partner of that partnership resided outside the United States for a period after the close of that taxable year and the tax matters partner later takes up residence within the United States, no notice may be mailed under paragraph (b) of this section while the tax matters partner resides within the United States.

(d) *No disallowance in certain circumstances.* If the person to whom the notice referred to in paragraph (b)(2) of this section is mailed establishes to the satisfaction of the Internal Revenue Service—

(1) That the losses and credits arising from the partnership for the year are proper; and

(2) That the partner has made a good faith effort to have the partnership file the required return; the Internal Revenue Service may allow the losses and credits in whole or in part.

(e) *Effective date.* This section is applicable to partnership taxable years beginning on or after October 4, 2001. For years beginning prior to October 4, 2001, see § 301.6231(f)-1T contained in 26 CFR part 1, revised April 1, 2001.

[T.D. 8965, 66 FR 50563, Oct. 4, 2001]

#### § 301.6233-1 Extension to entities filing partnership returns.

(a) *Entities filing a partnership return.* Except as provided in paragraph (c)(1) of this section, the provisions of subchapter C of chapter 63 of the Internal Revenue Code (subchapter C) and the regulations thereunder shall apply with respect to any taxable year of an entity for which such entity files a partnership return as well as to such entity's items for that taxable year and to any person holding an interest in such entity at any time during that taxable year. Any final partnership administrative adjustment or judicial determination resulting from a proceeding under subchapter C with respect to such taxable year may include a determination that the entity is not a partnership for such taxable year as well as determinations with respect to all items of the entity that would be partnership items, as defined in section 6231(a)(3) and the regulations there-

under, if such entity had been a partnership in such taxable year (including, for example, any amounts taxable to an entity determined to be an association taxable as a corporation). For example, a final determination under subchapter C that an entity that filed a partnership return is an association taxable as a corporation will serve as a basis for a computational adjustment reflecting the disallowance of any loss or credit claimed by a purported partner with respect to that entity.

(b) *Partnership return filed but no entity found to exist.* Paragraph (a) of this section shall apply where a partnership return is filed for a taxable year but it is determined that there is no entity for such taxable year. For purposes of applying paragraph (a) of this section, the partnership return shall be treated as if it were filed by an entity. However, any final partnership administrative adjustment or judicial determination resulting from a proceeding under subchapter C with respect to such taxable year may also include a determination that there is no entity for such taxable year.

(c) *Exceptions.* Paragraph (a) of this section shall not apply to—

(1) Entities for any taxable year in which such entity would be excepted from the provisions of subchapter C of the Internal Revenue Code under section 6231(a)(1)(B) and the regulations thereunder (relating to the exception for small partnerships) if such entity were a partnership for such taxable year; and

(2) Entities for any taxable year for which a partnership return was filed for the sole purpose of making the election described in section 761(a).

(d) *Effective dates.* This section is applicable to partnership taxable years beginning on or after October 4, 2001. For years beginning prior to October 4, 2001, see § 301.6233-1T contained in 26 CFR part 1, revised April 1, 2001.

[T.D. 8965, 66 FR 50563, Oct. 4, 2001]

#### § 301.6241-1T Tax treatment determined at corporate level.

(a) *In general.* For a taxable year of an S corporation beginning after December 31, 1982, a shareholder's treatment of a subchapter S item (as defined

in § 301.6245-1T) on the shareholder's return may not be changed except as provided in sections 6241-6245 of the Code and the regulations thereunder. Thus, for example, if a shareholder treats an item on the shareholder's return consistently with the treatment of that item on the S corporation return, the Internal Revenue Service generally cannot adjust the treatment of that item on the shareholder's return except through a corporate-level proceeding. Similarly, the shareholder may not put a subchapter S item in issue in a proceeding relating to nonsubchapter S items. For example, the shareholder may not offset a potential increase in taxable income based on changes in nonsubchapter S items by a potential decrease based on subchapter S items.

(b) *Restrictions inapplicable after items become nonsubchapter S items.* Section 6241 and paragraph (a) of this section cease to apply to items arising from an S corporation with respect to a shareholder when those items cease to be subchapter S items with respect to that shareholder under section 6231(b)(1) (as extended to and made applicable to subchapter S items under section 6244).

(c) *S corporation*—(1) *In general.* For purposes of subchapter D of chapter 63 of the Code, except as provided in paragraph (c)(2) of this section, the term "S corporation" means any corporation required to file a return under section 6037(a).

(2) *Exception for small S corporations*—

(i) *Effective date.* This paragraph (c)(2) shall apply to any taxable year of an S corporation the due date of the return for which (determined without regard to extensions) is on or after January 30, 1987.

(ii) *Five or fewer shareholders.* For purposes of this paragraph (c), an S corporation shall not include a small S corporation. A small S corporation is defined as an S corporation with 5 or fewer shareholders, each of whom is a natural person or an estate. For purposes of this paragraph (c)(2), a husband and wife (and their estates) are treated as one shareholder. If stock (owned other than by a husband and wife) is owned by tenants in common or joint tenants, each tenant in common or joint tenant is considered to be

a shareholder of the corporation. The limitation is applied to the number of natural persons and estates that were shareholders at any one time during the taxable year of the corporation. Thus, for example, an S corporation that at no time during the taxable year had more than 5 shareholders may be treated as a small S corporation even if, because of transfers of interests in the corporation, 6 or more natural persons or estates owned stock in the corporation for some portion of the taxable year.

(iii) *Special rule.* The exception provided in paragraph (c)(2)(ii) of this section does not apply to an S corporation for a taxable year if any shareholder in the corporation during that taxable year is a pass-through shareholder. For purposes of this paragraph (c)(2)(iii), a pass-through shareholder is—

(A) A trust;

(B) A nominee; or

(C) Other similar pass-through persons through whom other persons have an ownership interest in the stock of the S corporation. For purposes of the preceding sentence, a shareholder's estate shall not be treated as a pass-through shareholder.

(iv) *Determination made annually.* The determination of whether an S corporation meets the requirements for the exception under paragraph (c)(2)(ii) of this section shall be made for each taxable year of the corporation. Thus, an S corporation which does not qualify as a small S corporation in one taxable year may qualify as a small S corporation in another taxable year if the requirements for the exception under paragraph (c)(2)(ii) of this section are met with respect to that other taxable year.

(v) *Election to have subchapter D of chapter 63 apply*—(A) *In general.* Notwithstanding paragraph (c)(2)(ii) of this section, a small S corporation may elect to have the provisions of subchapter D of chapter 63 of the Code apply with respect to that corporation.

(B) *Method of election.* A small S corporation shall make the election described in paragraph (c)(2)(v)(A) of this section for a taxable year of the corporation by attaching a statement to the corporate return for the first taxable year for which the election is to be

effective. The statement shall be identified as an election under § 301.6241-1T(c)(2)(v)(A), shall be signed by all persons who were shareholders of that corporation at any time during the corporate taxable year to which the return relates, and shall be filed at the time (determined with regard to any extensions of time for filing) and place prescribed for filing the corporate return.

(C) *Years covered by election.* The election shall be effective for the taxable year of the corporation to which the return relates and all subsequent taxable years of the corporation unless revoked with the consent of the Commissioner.

[T.D. 8122, 52 FR 3002, Jan. 30, 1987]

#### § 301.6245-1T Subchapter S items.

(a) *In general.* For purposes of subtitle F of the Internal Revenue Code of 1986, the following items which are required to be taken into account for the taxable year of an S corporation under subtitle A of the Code are more appropriately determined at the corporate level than at the shareholder level and, therefore, are subchapter S items:

(1) The S corporation aggregate and each shareholder's share of, and any factor necessary to determine, each of the following:

(i) Items of income, gain, loss, deduction, or credit of the corporation;

(ii) Expenditures by the corporation not deductible in computing its taxable income (for example, charitable contributions);

(iii) Items of the corporation that may be tax preference items under section 57(a) for any shareholder;

(iv) Items of income of the corporation that are exempt from tax;

(v) Corporate liabilities (including determinations of the amount of the liability, whether the corporate liability is to a shareholder of the corporation, and changes from the preceding year); and

(vi) Other amounts determinable at the corporate level with respect to corporate assets, investments, transactions, and operations necessary to enable the S corporation or the shareholders to determine—

(A) The general business credit provided by section 38;

(B) Recapture under section 47 of the credit provided by section 38;

(C) Amounts at risk in any activity to which section 465 applies;

(D) The depletion allowance under section 613A with respect to oil and gas wells;

(E) Amortization of reforestation expenses under section 194;

(F) The credit provided by section 34 for certain uses of gasoline and special fuels; and

(G) The taxes imposed at the corporate level, such as the taxes imposed under section 56, 1374, or 1375;

(2) Any factor necessary to determine whether the entity is an S corporation under section 1361, such as the number, eligibility, and consent of shareholders and the classes of stock;

(3) Any factor necessary to determine whether the entity has properly elected to be an S corporation under section 1362 for the taxable year;

(4) Any factor necessary to determine whether and when the S corporation election of the entity has been revoked or terminated under section 1362 for the taxable year (for example, the existence and amount of subchapter C earnings and profits, and passive investment income); and

(5) Items relating to the following transactions, to the extent that a determination of such items can be made from determinations that the corporation is required to make with respect to an amount, the character of an amount, or the percentage of stock ownership of a shareholder in the corporation, for purposes of the corporation's books and records or for purposes of furnishing information to a shareholder:

(i) Contributions to the corporation; and

(ii) Distributions from the corporation.

(b) *Factors that affect the determination of subchapter S items.* The term "subchapter S item" includes the accounting practices and the legal and factual determinations that underlie the determination of the existence, amount, timing, and characterization of items of income, credit, gain, loss, deduction, etc. Examples of these determinations are: The S corporation's method of accounting, taxable year,